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May 23, 2002

The Honorable Harvey Pitt
Chairman
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D.C. 20545

Dear Mr. Chairman:

I am writing to follow up on remarks you made at the Commission's recent investor summit regarding private actions against aiders and abettors of securities fraud. I commend the Commission for holding its first summit under your chairmanship, and I hope that the Commission will continue, on a regular basis, to provide investors with opportunities to ask Commission leadership questions during similar public fora in the future.

As you noted during the summit, the Supreme Court's decision in *Central Bank of Denver N.A. v. First Interstate Bank of Denver* has precluded private parties from recovering damages from those who assist in the perpetration of fraudulent activities. Recent investigations into the collapse of the Enron Corporation and Global Crossing have illuminated the key supporting role that professional services firms sometimes play in the design, implementation and validation of fraudulent activities conducted by their clients. In their responses to the consolidated complaint in the pending Enron litigation, professional services firms frequently have cited the *Central Bank* precedent as they seek to have the charges against them dismissed, arguing that aiders and abettors are immune from liability for fraud alleged in private suits. For example, Merrill Lynch's motion to dismiss states, in relevant part:

> "[I]n recent years two developments have effected tectonic shifts in the law governing federal securities fraud actions, especially those pled not against the issuer of the securities in question but rather against the peripheral professional organizations who provided services to the issuer. Those two developments were (a) the enactment of the Private Litigation Securities Reform Act (sic) . . . and (b) the Supreme Court's decision in *Central Bank of Denver N.A. v. First Interstate Bank of Denver*, which overruled a generation of case law . . . under which lower courts had implied a private right of action for plaintiffs in securities fraud cases against defendants for 'aiding and abetting' a fraud committed by others . . . The Section 10(b) claims alleged against Merrill Lynch

must be dismissed . . . [because] plaintiffs' principal theory of liability against Merrill Lynch . . . is precluded by the Supreme Court's holding in *Central Bank.*"

While it remains to be seen whether such arguments will prove decisive in this case, *Central Bank* nevertheless poses a significant risk to investors who, defrauded by a firm that subsequently became insolvent, may be deprived of recovering losses from the remaining entities that helped to enable the fraud to occur in the first place.

I was encouraged by your comments at the investors summit about the need to investigate whether inoculation of aiders and abettors against liability alleged by private parties is precluding meritorious claims. I found particularly noteworthy your statement that "If investors are not being given a fair shake at those who really should be held accountable than the law has to be changed" and your pledge to collaborate with the AFL-CIO and others to further explore this important area: "There's no question that we'd be willing to work with you in looking at that issue to see if we can do something that meets all of our senses of what needs are in the area." With an estimated $3 billion in losses suffered by state pension systems as a result of the Enron debacle and investors nationwide facing unlikely prospects of recovery due to the insolvency of the alleged primary violator, the Commission's leadership in this area is especially needed at this time. I appreciate your willingness to consider changes in the securities laws to address this matter, and I have several questions regarding the Commission's plans.

1. You may know that I have introduced H.R. 3617, the Accountability for Accountants Act, which contains a provision that restores aiding and abetting liability, effectively overturning the *Central Bank* decision. In light of your recent comments, does the Commission:

   (A) Endorse legislative efforts to restore the ability of private parties to hold liable those who aid or abet others who commit fraud?
   (B) Intend to address, through regulation or other means, the inability of private parties to recover losses from aiders and abettors? If so, how? If not, why not?
   (C) Remain at all concerned that the *Central Bank* precedent may be shielding from liability those entities that provide integral, albeit supporting, services to the primary perpetrators of securities fraud?

2. While private parties are precluded from pursuing aiders and abettors, in your comments at the summit you emphasized that the Commission has endeavored to disgorge funds from those who aid and abet securities fraud. As you know, the Commission's ability to pursue such cases remains intact due to congressional action.

   (A) Since you were appointed Chairman, how many proceedings (e.g., inquiries, enforcement actions, litigation) has the Commission undertaken against alleged aiders and abettors of securities fraud?
   (B) Which firms or individuals were the subject of these actions? What was the result of each action, if the matter has been concluded as of May 1, 2002?

(C) For matters which have been concluded by May 1, what is the dollar amount recovered by investors as a result of the Commission's actions?
(D) Given the limitations on the Commission's resources and personnel, which inevitably preclude the SEC from bringing cases against all potential aiders and abetters of a securities fraud, do you believe that private plaintiffs should be permitted to sue those who have aided and abetted a securities fraud?

3. Since the 1994 Supreme Court decision in *Central Bank*, new technologies, new services – indeed, entire new industries – have emerged that have created new opportunities to perpetrate elaborate frauds, which may require the expertise of specialists with particular knowledge and skills to effectuate. With such intricate schemes, it is becoming increasingly difficult to discern where aiding and abetting ends and actual fraudulent activity begins.

(A) Almost a decade after *Central Bank*, does the Commission believe that this landmark judicial decision has furthered or undermined the objective of protecting investors and maintaining the integrity of the securities markets? If yes, how?
(B) Given *Central Bank's* bar against private parties recovering losses from aiders and abettors of fraud, from where does the Commission envision such parties will be able to seek damages when the primary violator of fraud has become insolvent?

I appreciate the Commission's responses to the issues I have raised above. Please provide the responses within fifteen business days, or no later than June 13, 2002. If you have any questions, please have a member of your staff contact Mr. Jeff Duncan or Mr. Mark Bayer of my staff at 202-225-2836.

Sincerely,

Ed Markey

Edward J. Markey
Member of Congress